made by certain states in opening up their local telecommunications markets by interpreting the 1996 Act in a way that would hamper competition. Guidance from the Commission on the correct interpretation of these key pricing guidelines will benefit state commissions and carriers by reducing the need for lengthy state commission proceedings to interpret the 1996 Act.

Moreover, establishing national pricing principles should preclude the creation of pricing rules that frustrate (intentionally or otherwise) the development of local competition. For example, the Texas Public Utility Commission has promulgated an interconnection rule that specifically allows the reciprocal compensation rate for local traffic to vary depending on the Extended Area Service and Extended Local Calling Area plans available to incumbent LEC customers for local traffic over specific routes.[58] Clearly, a Transport and Termination rate that varies depending upon incumbent LEC local calling plans does not provide the stable rate structure required by a new entrant to commit to investment in facilities, and does not meet the statutory requirements for an appropriate

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*Telecommunications Act of 1996*, Docket No. UT-960269 (Washington Utilities and Transportation Commission).

58. The practical result of the Texas rule is that the ILECs will be able to charge CLECs switched access rates -- rather than rates based on the "additional cost" of carrying the traffic as required by the 1996 Act for portions of Transport and Termination. As a consequence CLECs will be precluded by a price squeeze from carrying traffic over any route for which the new entrant must compensate the ILEC at switched access rates.

Transport and Termination rate. Similar barriers may arise in other states unless the Commission prescribes firm pricing guidelines.

### B. What pricing standards should the Commission adopt? (NPRM ¶¶ 122-157)

TCG agrees with the Commission's tentative conclusion that the pricing principle adopted for physical interconnection, unbundled network elements, and collocation should be the same. Moreover, the Commission is correct in its view that the states cannot set rates for interconnection and network elements based on historical costs incurred by ILECs, since those would be costs that have been "determined with reference to a rate-of-return or other rate-based proceeding." Rather, TCG advocates the use of a forward-looking incremental cost methodologies. Such standards do not involve the use of embedded costs, which are not appropriate because they do not reflect the forward-looking economic cost of providing a product or service.

There are significant differences in the costing methodologies adopted in various states, and there is no one state model that the FCC can adopt for all purposes.[59] It is, however, clearly in the public interest for the Commission to

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59. Indeed, there are some state costing approaches that appear clearly at odds with the requirements of the 1996 Act. For example, the New York Public Service Commission proposals to account for "contribution loss" and the impacts of "stranded plant" are inconsistent with the 1996 Act. First, "contribution" is a rate-of-return concept which assumes that a subsidy to local exchange service exists, and thus conflicts with the 1996 Act's separate treatment of universal service, as well as its rejection of rate-of-return based costing. Second, it is

create a national, consistent standard (or "preferred outcome") for costing and pricing interconnection, network elements, and collocation. This would conserve the resources of state commission and parties by avoiding the need to continually re-litigate common costing issues, and encourage productive and fair negotiations between CLECs and ILECs.

One of the important issues the Commission will have to address is the definition and allocation of common costs. Common (or shared) costs are those costs incurred in the production of a group of services or elements but which are not caused by any single service or element. Because they cannot be linked uniquely and directly to any particular service, common costs must be allocated in a competitively-neutral manner among the relevant services. The chief risk in the identification and assignment of common costs is that ILECs have an incentive to allocate common costs to services with the least elastic demand, that is, services that are considered essential by subscribers, and for which no substitute is available. Thus, subscribers to a price-inelastic service are highly unlikely to discontinue their services even though the price increases. This would result in an excessive assignment of costs to largely captive monopoly residential and small

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unclear that ILEC plant will be stranded at all, given that the ILEC is able to offer it for resale, or sell it to a competitor outright, thereby recovering its costs. Third, it is unlikely that facilities-based alternatives to the incumbent local exchange carriers will develop so rapidly as to render any existing ILEC plant useless or "stranded." An offset for "contribution" loss is nothing more than a relic of the much-discredited "efficient component pricing rule," which the Commission has rightly dismissed (NPRM ¶147).

business subscribers, who currently have no facilities-based competitive local exchange alternatives. Indeed, it is this Commission's responsibility, and challenge, to make the correct policy choices here so that those subscribers do have a choice in the future.

TCG does not believe, however, that it would be appropriate to differentiate costs based on geographic or class of service categories. As noted in TCG's discussion of unbundled elements, *supra* Part IV, TCG does not believe that loops or other network elements that can be used to carry different types or classes of services should be costed differently depending on use. Similarly, TCG does not believe that there is typically a basis in cost causation to support a geographic or class of service disaggregation of multi-use facilities -- many of these classifications are largely Marketing or Regulatory distinctions that have no basis in cost characteristics.

**C. "Pay or Play" Type Pricing Approaches (NPRM ¶ 145).**

The Commission seeks comment on whether it is appropriate to recover universal service or other subsidies in interconnection, collocation, and unbundled element rates.[60] TCG strongly opposes the use of such rates to support universal service or otherwise subsidize the ILEC's operations. The 1996 Act clearly

60. TCG notes that the Commission does not include Transport and Termination among the services to be used for such support payments, and presumes that the Commission recognizes that the "additional cost" standard of the 1996 Act flatly and clearly prohibits such rate structures. §252(d)(2).

requires an explicit mechanism for the support of universal service.[61] The 1996 Act is equally explicit with respect to the pricing standards for interconnection elements.[62] The so-called "Pay-or-Play" compensation model developed in New York prior to the enactment of the 1996 Act satisfies neither of these provisions, and the Commission should unequivocally prohibit "Pay- or-Play" in any form.[63]

"Pay or play" is not the only method by which states are establishing pricing standards that are inconsistent with the 1996 Act. For example, in Texas unbundled loops are required to be priced on a usage-sensitive basis in the Texas Public Utility Regulatory Act ("PURA").[64] This usage pricing requirement in PURA has allowed Southwestern Bell to inflate its costs for unbundled loops. Southwestern performed a cost study in compliance with the statute that resulted in a flat-rate per loop cost for unbundled loops. It then calculated a MOU charge by dividing the flat-rate per loop estimated cost by a low assumed average per month minutes of use. The result was a high MOU charge which, multiplied times the actual per month minutes of use, would result in a high unbundled loop price

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61. *See* §254(e).

62. *See* §252(d)

63. For a more detailed discussion of the "pay or play" concept, *see* TCG's Comments in the FCC's Universal Service proceeding, Docket CC 96-45.

64. Tex. Rev. Civ. Stat., Art 1446c-O, §3.453.

that is not properly cost-based.[65] The Commission should mandate that all existing state statutes and rules that set non-cost based rates for loops cannot be enforced as they are preempted by the 1996 Act.

Requirements that carriers serve particular geographic areas, serve particular classes of customers, or have a "customer mix" comparable to or identical to the ILEC, are other ways that "universal service" type conditions can be imposed on new entrants. Such obligations, if imposed as a condition of the license or as a requirement to receive lower cost interconnections, would be a barrier to entry prohibited under §253 of the 1996 Act.

**D. Capacity Based Costs and Prices.**

Many of the facilities and services that ILECs provide to CLECs incur costs based on changes in capacity, rather than based on individual calls or minutes of use. It is for that reason that bill and keep, or other capacity based charges, are the best approach for Transport and Termination, as discussed below.[66] The Commission properly notes that the Washington Utilities and Transportation Commission has determined that measured-use interconnection rates are inappropriate when applied to the capacity based cost of terminating local traffic.

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65. *See, Applications of Southwestern Bell Telephone Company, GTE Southwest, Inc. And Contel of Texas, Inc. For Usage-sensitive Loop Resale Tariffs Pursuant to PURA 1995 §3.453*, Docket No. 14569 (Public Utility Commission of Texas).

66. "Bill and keep" can be regarded as a Transport and Termination arrangement with a capacity cost of zero.

The WUTC pointed out that usage-based rates would create a disincentive to offer flat-rated calling services. Allocation of costs based on capacity is inherently more efficient, as it places the responsibility for maximizing network efficiencies on the purchaser of the facility and thus ensures that new facilities will not be added until it is economically sensible to do so.

## VI. ILEC OBLIGATION TO INTERCONNECT IXCs, CMRS, AND NONCOMPETING ADJACENT LECS (NPRM ¶¶ 158-171)

### A. Are interconnection agreements between ILECs and non- competing neighboring LECs subject to Sec. 251(c)(2)? If so, must the agreements be made public? (NPRM ¶¶ 170-171)

TCG agrees with the Commission's tentative conclusion that the interconnection requirements set forth in §251 of the 1996 Act include interconnection agreements between the ILECs and non-competing neighboring ILECs.[67] The 1996 Act expressly covers all interconnections between carriers, and nowhere does the 1996 Act differentiate between competing and non-competing ILECs. Accordingly, interconnection agreements between ILECs and non-competing ILECs are subject to the same filing requirements as all other ILEC/LEC interconnection agreements, as set forth in §251(h) and (i).

Such agreements, once filed, may prove valuable in providing a framework for interconnection. TCG considers it significant that the ILECs, in every instance, have insisted on implementing interconnection arrangements with CLECs which are

67. TCG presumes that the Commission's reference to "non-competing neighboring LECs" is intended to refer to "non-competing, neighboring ILECs."

substantially different in nature and economics from the interconnection arrangements established between neighboring or affiliated ILECs. The interconnection arrangements between the ILECs were established in an environment in which the two entities did not expect to compete with each other. Presumably these arrangements are competitively neutral, and would be less characterized by efforts to impede the operations of the interconnecting parties. The ILECs' insistence on a different arrangement for CLECs suggests that the ILECs are attempting to secure a competitive advantage through the interconnection process.

TCG has in fact attempted to use these pre-existing interconnection agreements as a departure point for its interconnection negotiations. TCG sent letters to ILECs requesting that they provide TCG with a representative sample of these interconnection agreements, explaining that if the terms of those agreements were acceptable for interconnection purposes it would save the parties the effort of negotiating those issues. TCG explained that there was no point in "reinventing the wheel" if the existing interconnection agreements could be used. With only one exception, the ILECs refused to make such agreements available to TCG. Only NYNEX actually provided any agreements, although in doing so it stated that it did not regard these agreements as relevant to TCG's negotiations. Additionally, at least one RBOC (Ameritech) has taken the additional step of attempting to suppress these prior interconnection agreements by sending notices to independent telephone companies stating that it was unilaterally canceling the agreements.[68]

One thing that the Commission can do, which could speed the negotiation process, would be to require the LECs to lift the veil of secrecy surrounding their arrangements with the independent telephone companies (or with their affiliated local exchange carriers) and make these arrangements public. Since the 1996 Act requires the RBOCs to submit their existing contracts with independent telephone companies for approval (Sec. 252(a)(1)), this does not impose any additional burden on ILECs. Therefore, the Commission should require that all ILEC interconnection agreements, including agreements with non-competing, neighboring ILECs (including affiliated companies) must be made public and available to other telecommunications carriers.[69]

Additionally, to address the question of whether the ILECs have recently renegotiated previous arrangements, the Commission should require that the ILECs also submit agreements that were effective within the 24 months preceding the enactment of the 1996 Act. The Commission should further declare that CLECs are permitted to utilize, in whole, any interconnection arrangements offered under those agreements.

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68. *See, e.g.,* Letter of Association for Local Telecommunications Services to Cheryl L. Parrino, Chairman, Wisconsin Public Service Commission, April 1,1996

69. Indeed, the Commission has authority to require the such agreements be filed under its preexisting statute. *See* §211.

### B. Under what conditions should other carriers be allowed to utilize provisions of other carrier's interconnection agreements? (NPRM ¶ 170)

There is a broader question about the extent to which CLECs should be permitted to benefit from interconnection agreements negotiated by other CLECs. TCG believes that whether CLECs should be permitted to take service pursuant to interconnection agreements negotiated or arbitrated by other carriers will depend in part on whether the Commission has established the appropriate "preferred outcomes" so that meaningful negotiations can take place. If that is the case, then all carriers will have an opportunity to negotiate reasonable terms, and should only be allowed to take service pursuant to another carrier's agreements subject to the full scope of the contract and the reasonable terms and conditions thereof. Allowing carriers to "pick and choose" **individual rates or terms from multiple agreements could tend to inhibit parties from making "trade offs" of different "preferred outcomes," if a package of such "trade offs" can later be taken apart and the individual pieces of the bargain taken by another party.**[70] On the other hand, if the Commission does not implement a strong set of preferred outcomes, then the Commission should allow carriers to "pick and choose" from other

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70. At the same time, ILECs should not be allowed to "fence off" interconnection agreements in order to prevent their use by other carriers by incorporating restrictive terms that are not truly germane to the service being provided and are intended primarily as means to limit the availability of the arrangement to other interested parties. TCG would put in that class, for example, an agreement that was limited to non-overlapping traffic -- ILECs should not be allowed to negotiate agreements that differentiate on that basis, since there is no foundation in the 1996 Act for such a requirement.

carrier's agreements, since in the absence of the more equal bargaining conditions under a preferred outcomes approach there will be little real negotiation possible that can be inhibited, and allowing carriers to pick and choose elements of other carrier's agreements (particularly ILEC-ILEC agreements) may be the only way that a CLEC will be able to assemble a complete interconnection agreement.

## VII. ILEC RESALE OBLIGATIONS (NPRM ¶¶ 172-188)

### A. Resale Obligations (NPRM ¶ 174)

The Commission tentatively concludes that all LECs have an obligation to allow resale of services, but only ILECs are subject to wholesale pricing standards. The Commission is correct. Section 251(b)(1) requires that all local exchange carriers, including incumbent LECs and CLECs, permit resale, but does not itself impose any pricing standards. Section 251(c)(4) imposes an additional duty on ILECs to offer for resale at wholesale rates any telecommunications services that it provides at retail to subscribers who are not telecommunications carriers. Section 251(c)(4) thus applies only to ILECs and does not apply to CLECs.

### B. Avoided Cost Standards (NPRM ¶¶ 179-183)

The Commission asks whether it should enunciate a set of national "presumptions" that would apply to the question of what should be the definition of "avoided costs."

TCG's view is that some national standardization on this issue is essential to establish general parameters of what should be considered to be an avoided cost, while leaving to the parties in negotiation the precise quantification of the costs that are avoided.

One of the difficulties in attempting to enunciate precise costing rules in this area is that the FCC's existing costing information is simply not sufficiently precise to be used to calculate avoided costs. The FCC's basic cost information is "category" or functional cost information, rather than service specific information. Thus while the current ARMIS information filed with the Commission can adequately allow the FCC to identify, for example, the total amount of marketing expenses of an ILEC, it does not provide any exact information (for example) on the amount of marketing expenses (or any other expense, for that matter) that is associated with single line business exchange service, much less the proportion that is going to be "avoided" as a result of a reseller buying that service. Accordingly, the FCC is not positioned to enunciate a specific and detailed cost rule or model, but it can and should identify some general guidelines and rules that could be used to calculate the costs that will be avoided.

For example, one standard that the Commission could adopt is that avoided costs do not include any "share of general overhead or 'mark-up' assigned to such costs." NPRM at ¶ 180. The statutory standard focuses on costs that will actually be "avoided." Such a standard would not appear to reasonably include overhead costs, since an overhead cost is a general cost that -- by definition -- is not directly attributable to the delivery of a particular unit of demand, and thus --

almost by definition -- cannot be "avoided" by converting a particular unit of demand from a retail sale to a wholesale transaction. Stated another way, the cost of the CEO's desk is the same whether a particular local exchange line is sold at retail versus wholesale, and thus this is not a cost that is "avoided" by the wholesale transaction.

Another standard that the Commission should use is that avoided costs represents the "net" of the costs that will be avoided, rather than the gross amount of costs that are "displaced." Stated another way, the billing cost that is avoided on a wholesale transaction represents the gross amount of retail billing cost that is made unnecessary as a result of the fact that the service will be sold at wholesale, less the billing costs that are incurred to provision the service on a wholesale basis. For example, only the billing costs that will actually be "avoided" -- not the larger gross amount of billing costs that have been "displaced" by the wholesale transaction -- are to be considered in the calculation of avoided costs. To do otherwise would be to require that other customers must pay for the costs incurred solely to provide services to wholesale customers, which would be inconsistent with basic principles of cost causation.

Additionally, the Commission should not presume, as some have suggested, that there will be no "uncollectibles" with wholesale services, and therefore all of the costs associated with that aspect of business can be ignored. While the use of a wholesale transaction eliminates the risk to the underlying carrier that the retail end user will not pay his or her bills, that does not eliminate the risk to the underlying carrier that the wholesaler will not pay *its* bills. Thus uncollectibles will continue to be a "cost" to the underlying carrier. While the gross amount of uncollectibles that would be experienced in the retail market will be avoided, a new uncollectibles risk will be introduced, and in fact may well be greater for wholesale than for retail sales.

The Commission should also establish some basic guidelines for the calculation of avoided costs. The statute enumerates four kinds of expenses that might be avoided: "marketing, billing, collection and other costs." §252(d)(3). This Commission should declare that marketing, billing and collection costs can be presumed as costs that will be avoided to some degree, subject to an appropriate demonstration by the ILEC as to the amount of costs that will be avoided, while any other cost categories should not be presumed to be avoided absent further justification. Such a justification should include a detailed demonstration that there is a clear difference in the manner in which wholesale service is provided versus retail service that, in the case of the other cost characteristic, can reasonably be demonstrated to lead to net cost savings to the ILEC.

Establishment of some national guidelines would avoid inconsistent state results. For example, TCG believes that the Illinois Commerce Commission ("ICC") Staff proposal for wholesale rates is inconsistent with the 1996 Act.[71] The Staff

71. NPRM at ¶ 183.

has proposed that the wholesale price for local resold services should be set at "equal to the retail price less net total assigned cost of retail functions less a pro rata share of contribution attributable to the avoided retail functions. This approach attributes a pro rata share of contribution to the avoided retail functions."[72] The effect of this approach is to set the contribution level generated by wholesale rates at the same proportionate level as exists in retail service rates, given the underlying costs of each service. According to ICC Staff's own evidence presented in ICC Docket No. 95-0458, an appropriate level of discount for a local wholesale offering, based upon an avoided cost analysis, is approximately 8.7%.[73] Under ICC Staff's pro rata contribution methodology, however, the discount more than doubles to 18.3%.[74] ICC Staff's pro rata share of contribution methodology is not an appropriate local wholesale pricing mechanism under the 1996 Act, since it is based in part on "avoided contribution" not avoided costs. The Commission therefore should declare that such wholesale pricing approaches violate the 1996 Act.

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72. Staff Brief, Illinois Commerce Commission, Docket No. 95-0458, at 20.

73. Transcript of Hearing, p. 493.

74. *Id.*

### C. Unbundled Elements, Price Squeezes, and Imputation Tests (NPRM ¶¶184-188)

The Commission raises an important issue in addressing its concerns about the relationship between costs for unbundled elements versus costs for wholesale and retail elements, and the role of imputation tests.[75] There is, in fact, a real and substantial risk that the development of facilities-based local competition can be adversely affected if wholesale or retail rates are priced inequitably relative to unbundled element costs, creating an uneconomic price squeeze.

The relationship between wholesale rates and facilities-based competition has been addressed by the Connecticut Department of Public Utility Control ("DPUC"), and TCG believes that the policy questions that DPUC raised are instructive for this Commission to consider. The DPUC, for example, stated that "[a wholesale] cost and associated price that is too low will greatly increase the level of financial benefit presented to prospective providers by resale competition and discourage the development of alternative telecommunications infrastructure in Connecticut, possibly limiting the choice of services and providers intended by passage of Public Act 94-83."[76] The Department further stated that:

> "[wholesale] rates and charges that are set too low will only prolong the existence of a resale market and retard the eventual development of

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75. NPRM at ¶ 184-188.

76. *Application of the Southern New England Telephone Company for Approval to Offer Unbundled Loops, Ports and Associated Interconnection Arrangements*, Docket No. 95-06-17, (December 7, 1995), p. 75.

> facilities-based competition in Connecticut. Unbundled loops, ports and interoffice facilities are needed and necessary as a transition vehicle to facilities-based competition and must be priced as such to meet that objective. The Department will ensure that its efforts to achieve a framework for strategic competition are not lost to the expediency of resale."[77]

This Commission, too, must ensure that wholesale competition does not drive out or diminish the development of strong, facilities-based competition. It is clearly a driving principle of the 1996 Act that facilities-based competition is necessary for the existing, dominant local exchange carriers to be inhibited from engaging in anticompetitive pricing, service, installation and other practices. It is not surprising, for example, that the existence of facilities-based competition is at the center of the decision of whether the existing Bell operating companies can be permitted to enter the long distance markets in their territories.[78]

TCG notes, however, that the Commission expresses some doubts about whether to conduct an imputation test. It observes that the NYPSC has not adopted an imputation test, apparently on the assumption that although the ILEC will fail the test, the incumbent can somehow find enough revenues somewhere to make up the difference.[79] In a similar situation, however, the Illinois Commerce Commission ("ICC") reached a contrary conclusion. In that case, Illinois Bell had argued that it should be able to charge switched access rates for Transport and

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77. *Id.* at 77.

78. *See, e.g.*, 47 U.S.C. §271(c)(1)(A).

79. NPRM at ¶ 186.

Termination, even though those rates would put competitors in a clear cost-price squeeze. Illinois Bell argued that the competitors could collect money from other sources in order to afford the high switched access charges. The ICC rejected that argument, stating that, "The issue is not whether a new LEC ultimately can scrape together revenues from enough sources to be able to afford Illinois Bell's switched access charges. The crucial issue is the effect of a given Transport and Termination proposal on competition."[80] Finding the cost-price squeeze to be incompatible with a healthy competitive environment, the ICC rejected the Illinois Bell proposal.

The ICC was clearly correct. Assuming that a CLEC can find money elsewhere to pay for the "cash drain" of a price squeeze obviously assumes that the competitor will have equal access to all possible sources of funds to pay for the cost-price squeeze, that its margins will be equal or greater to those of the ILEC, and that it does not face cost-price squeezes in other markets as well. The obvious competitive disequilibriums that such an analysis must lead to makes clear that the Commission cannot ignore the risk of cost price squeezes, or discard its best diagnostic tool -- imputation -- to detect them. Stated another way, the patient may still have a fever even if the doctor does not take his temperature -- but unless the doctor does so, it will be difficult to prescribe a course of treatment.

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80. *Illinois Bell Telephone Company Proposed Introduction of a Trial of Ameritech's Customer First Plan in Illinois*, Docket Nos. 94-0096, 94-0117, 94-0146, 04-0301 consol. at p. 98 (Illinois Commerce Commission, April 7, 1995).

And unless this Commission "takes the temperature" of the ILEC's prices by applying an imputation test, it will not know if the market conditions are healthy or not.

To ensure that facilities-based competition takes root, the Commission must require that ILECs pass an imputation test, comparing their retail and wholesale rates with the physical interconnection, loop, switching capacity, and Transport and Termination rates that a competitor would incur to offer an equivalent service. With respect to the remedies that should apply if a carrier fails an imputation test, TCG believes it is unwise to try to enumerate the relief that will be accorded until the Commission has had the opportunity to examine the facts of the case. At a minimum, the Commission should, as part of its "public interest" determination under §271 of the 1996 Act, condition an RBOC's satisfaction of the unbundling requirement for entry into the intra-region long distance market for a state on its passing of imputation tests in that state, for if the market is characterized by cost-price squeezes it cannot be considered to be sufficiently competitive to allow entry.

## VIII. TRANSPORT AND TERMINATION

### A. Who and What is Entitled to Transport and Termination? (NPRM ¶¶ 226-229)

TCG agrees with the Commission's position that Transport and Termination encompasses LEC-to-LEC telecommunications traffic,[81] i.e., connections between facilities-based local exchange carriers. To the extent that an interexchange carrier (IXC) functions as a facilities-based LEC in provisioning local exchange services, the IXC also should be obligated to provide and have the right to receive Transport and Termination for the LEC traffic so exchanged.[82]

The IXC's right to terminate local calls under a Transport and Termination arrangement, however, does not allow an IXC to completely bypass switched access services. First, nowhere in the 1996 Act is it stated that Transport and Termination arrangements are meant to override or replace switched access. Indeed, the overall intent of the sections of the 1996 Act addressed in this NPRM is to open up the *local* exchange market to competition -- after all, the long distance market has been subject to some competition since the 1970's and considerable competition since Divestiture.[83] To conclude that opening up the

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81. LEC-to-LEC traffic includes calling between neighboring and non-competing ILECs as well as between ILECs and CLECs. Moreover, in light of recent announcements by companies such as GTE and BellSouth of their plans to offer competing local exchange services in adjoining territories, the distinction between competing and non-competing LECs may be a short-lived one.

82. *See* §251(d)(2)(A).

83. *See United States v. AT&T*, 552 F. Supp. 131 (D.D.C. 1982).

local exchange market to competition requires a complete restructuring of the national long distance switched access regime defies logic.

Where the statute is silent or ambiguous, it is the responsibility of the agency, in this case the FCC, to make the final determination, provided its decision does not conflict with the overall intent of the statute.[84] The NPRM makes clear that the Commission wishes to address the restructuring of switched access pricing in a separate proceeding.[85]

TCG submits that the Commission should define the conditions under which the §252(d)(2) Transport and Termination rate applies. In determining when a carrier is entitled to interconnect pursuant to the reciprocal compensation provisions §251(b)(5), the Commission must require that (1) the carrier be the facilities-based local exchange carrier providing dial tone to the originating caller

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84. *See Chevron, U.S.A. v. Natural Resources Defense Council*, 467 U.S. 837, 843, 81 L. Ed. 2d 694, 104 S. Ct. 2778 (1984) (If a statute is silent or ambiguous with regard to a specific issue, then a reviewing court must accept the interpretation of the administrative agency so long as it is reasonable and is not contrary to the clear intent of Congress.); *Communications Workers v. Beck*, 487 U.S. 735, 769, 101 L. Ed. 2d 634, 108 S. Ct. 2641 (1988). *See also Nationwide Mut. Ins. Co. v. Cisneros*, 52 F.3d 1351 (6th Cir. Ohio 1995), *reh'g, en banc, denied*, 1995 U.S. App. LEXIS 21068 (6th Cir. Aug. 4, 1995), and *mot. granted, cert. denied*, 133 L. Ed. 2d 893, 116 S. Ct. 973 (U.S. 1996); *cf. Time Warner Cable v. Doyle*, 66 F.3d 867, 876 (7th Cir. Wis. 1995), *mot. denied, cert. denied, Doyle v. Time Warner Cable*, 133 L. Ed. 2d 894, 116 S. Ct. 974 (U.S. 1996) (Statutory language should be conclusive except if the literal application of a statute [or a section thereof] will produce a result demonstrably at odds with the intentions of its drafters. A literal construction is inappropriate if it would produce absurd results and would thwart the obvious purposes of the statute).

85. NPRM at ¶ 164.

and 2) the call must both originate and terminate within the same LATA -- which includes LATA-wide services.[86] This standard has a twofold purpose. First, it allows facilities-based LECs to receive just and reasonable compensation as required under §251(b)(5). In addition, it allows changes to long distance switched access to be evaluated independently of Transport and Termination of local calls. Simply put, only telecommunications carriers that provide facilities-based local exchange service are eligible for Transport and Termination under §252(d)(2).

With respect to reciprocal compensation for the Transport and Termination of traffic, the 1996 Act imposes on the Commission the obligation to set a rate solely based on the "additional costs of terminating" calls from another carrier's network. The foregoing is predicated on §252(d)(2)(A), which stipulates that State Commissions are not to consider the terms and conditions for Transport and Termination to be "just and reasonable" unless they meet the criteria set forth in §§252(d)(2)(A)(i) & (ii). Section 252(d)(2)(A)(i) requires mutual recovery for each carrier of the costs associated with the Transport and Termination on each carrier's network facilities of calls that originate on the network facilities of other carriers.

However, §252(d)(2)(A)(ii) "requires that such costs be determined "on the basis of a reasonable approximation of the additional costs of terminating such

86. The "L" in LATA stands for "Local." Sec. 153(43)(B) of the Communications Act, as amended by the 1996 Act, permits Bell Operating Companies, with the approval of the Commission, to redefine LATA boundaries.

call." Because §252(d)(2)(A)(i) requires that costs for "Transport and Termination" be based on the "additional costs" of termination (§252(d)(2)(A)(ii)), the costs of Transport and Termination must be determined based on a reasonable approximation of the additional costs of only terminating traffic from the point at which the traffic is handed off from one LEC to another. With respect to the transmission facilities used to connect carriers for purposes of exchanging "Transport and Termination" traffic, each carrier should therefore bear its own costs of interconnecting to the hand-off point.

### B. Bill and Keep Is the Transport and Termination Method of Choice for ILECs and CLECs. (NPRM ¶¶ 239-243)

Bill and keep is the most commonly used method in the telecommunications industry for ILEC-ILEC transport and termination.[87] It has been successfully used for decades to govern the relationships between larger ILECs, such as the Bell Operating Companies, and smaller independent telephone companies. In some cases, the "toll free" calling areas of the two carriers overlap, and the agreement therefore becomes an arrangement for the exchange of local traffic. In other cases, calls between customers in each company are treated as toll or extended area service calls, and are not considered to be within the ordinary local calling scope of customers, and such arrangements are generally referred to as "Extended

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87. *See, e.g., City Signal Inc.*, 159 PUR 4th 532 (1995) ("LECs in Michigan does not compensate each other for terminating local or EAS calls. Instead, they have a "bill and keep" arrangement...").

Area Service Agreements". However, to the best of TCG's knowledge, the basic principles of how these calls are exchanged -- the use of mid-span meet type arrangements and largely bill and keep compensation -- is common across the country.

There is no merit to the arguments raised by some ILECs that bill and keep is illegal because it does not represent any payment for services. The fact that the payment is "in kind" rather that "in cash" does not make the transaction any less lawful, nor does it lead to the conclusion that such a transaction can only be ordered as a "waiver" of compensation. In an "in kind" transaction both parties receive legal consideration: the completion of one another's calls. Indeed, taking the ILEC argument to its illogical conclusion would suggest that barter transactions for services (*e.g.*, businesses and individuals providing each other services but not cash) have no value. The United States Internal Revenue Service, however, recognizes barter transactions in determining income tax liability under the Internal Revenue Code.[88] Thus, payment in kind has true legal value -- even the IRS says it is so.

The list of jurisdictions where bill and keep (or the equivalent) has also been adopted to govern the exchange of traffic between ILECs and CLECs is long and growing longer:

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88. Treas. Reg. §1.61-2(d)(1).

In **California**, the Commission has required bill and keep for the first year of competition.[89]

In **Oregon**, the Commission required that bill and keep be used for at least for two years.[90]

In **Washington State**, the Commission required bill and keep as its initial interconnection standard.[91] The Washington decision is particularly important, because it engages in an extended analysis of the adverse market consequences of usage-sensitive interconnection arrangements, and the benefits of bill and keep.

In **Texas,**[92] bill and keep is the default form of mutual compensation for the first nine months after the date on which the first call is terminated between CLECs and ILECs.

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89. California Public Utilities Commission, *Order Instituting Rulemaking on Commission's Own Motion into Competition for Local Exchange Service; Order Instituting Investigation on the Commission's Own Motion into Competition for Local Exchange Service*, Decision No. 95-07-054, (July 24, 1995), Dkt. Nos. R.95-04-043 and I.95-04-044.

90. Oregon Public Utilities Commission, *Applications of Electric Lightwave, Inc. MFS Intelenet of Oregon, Inc., and MCI Metro Access Transmission Services, Inc.*, Order No. 96-021 (Jan. 12, 1996), Dkt. Nos. CP-1, CP-14, and CP15.

91. Washington Public Utilities Commission, *Fourth Supplemental Order Rejecting Tariff Filings and Ordering Refiling; Granting Complaints, in Part*, (Oct. 31, 1995), Dkt. No. UT-941464.

92. Texas' new telecommunications law, enacted in 1995, provides that for the first nine months of a competitive local telephone company's actual operations the reciprocal compensation method shall be bill and keep. *See* Tex. Rev. Stat. §3.458(c)(1995).